

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

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UNITED STATES OF AMERICA,

-against-

MEMORANDUM AND ORDER
04-CR-699 (DRH)(S-2)

RODNEY ARNOLDO MORRISON,

Defendant.

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A P P E A R A N C E S:

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HURLEY, Senior District Judge

The defendant Rodney Arnoldo Morrison ("defendant" or
"Morrison") stands convicted of conspiracy under the Racketeer

Influenced and Corrupt Organizations Act ("RICO") pursuant to 18 U.S.C. § 1962(d) as charged in Count Two of the second superseding indictment ("indictment"). More specifically, the jury found that he conspired to conduct the affairs of the Peace Pipe Smoke Shop (the "Enterprise" or "Peace Pipe")¹ through a pattern of racketeering via the sale of contraband cigarettes in violation of 18 U.S.C. § 2342(a).²

The government now seeks forfeiture in the form of a personal "money judgment . . . against the defendant" under Count Two "in accordance with 18 U.S.C. §§ 1963(a)(1) and (a)(3)('RICO forfeiture')." (Gov't's Mar. 6, 2009 Mem. of Law Regarding Certain Forfeiture Issues ("Gov't's Mar. 6, 2009 Mem.") at 1.) As a result, the Court is required to "determine the amount of money that the defendant will be ordered to pay." Fed. R. Crim. P. 32.2(b)(1). That determination is the subject of this opinion.

BACKGROUND

Familiarity with the facts and procedural background of

¹ The grand jury charged (indictment ¶ 3), and the trial evidence established that the Enterprise included not only the Peace Pipe but also smokersden.com, as well as the employees and associates of both entities and the defendant. Smokersden.com is the internet marketing component of Peace Pipe. For simplicity sake, I will, as indicated in the text, identify the Enterprise either by that term or simply as the Peace Pipe.

² The defendant was also convicted of illegal possession of a firearm in violation of 18 U.S.C. § 922(g)(1) as charged in Count Eight of the indictment.

this case is presumed. Thus, the Court states only those facts necessary for disposition of the instant matter. The Peace Pipe is a retail and wholesale marketer of untaxed cigarettes operating on the Poospatuck Indian Reservation located in Mastic, Suffolk County, New York. Although the business is owned by defendant's spouse Charolette Morrison (Gov't's Ex. 238 ¶¶ 4, 5; see also Gov't's Ex. 159b),³ it has been operated and otherwise solely controlled by the defendant during the relevant time period.

The racketeering acts underlying Morrison's RICO conspiracy conviction entail the knowing and intentional sale of "contraband cigarettes . . . lacking valid New York State tax stamps, in violation of Title 18, United States Code, Sections 2342(a) and 2" from January 8, 1997 to August 2, 2004.

(Indictment ¶ 21.) 18 U.S.C. § 2342(a) is part of the Contraband Cigarettes Trafficking Act ("CCTA"), 18 U.S.C. §§ 2341 et seq., and provides:

It shall be unlawful for any person knowingly to ship, transport, receive, possess, sell, distribute, or purchase contraband cigarettes or contraband smokeless tobacco.

18 U.S.C. § 2342(a). Contraband cigarettes are defined in

³ The language in the indictment, as well as the government's brief indicating that defendant was an "owner" of the Peace Pipe (indictment ¶ 2 and, e.g., Gov't's June 15, 2009 Reply Mem. of Law Regarding Certain Forfeiture Issues at 2), is inconsistent with the trial and hearing evidence.

§ 2341 as follows:

a quantity in excess of 60,000^[4] cigarettes, which bear no evidence of the payment of applicable State or local cigarette taxes in the State or locality where such cigarettes are found, if the State or local government requires a stamp, impression, or other indication to be placed on packages or other containers of cigarettes to evidence payment of cigarette taxes, and which are in the possession of any person other than [setting forth exempted persons]

Id. § 2341(2).

Article 20 of the New York State Tax Law imposes "a tax on all cigarettes possessed in the state by any person for sale, except that no tax shall be imposed on cigarettes sold under such circumstances that this state is without power to impose such tax" or on certain sales to the United States. N.Y. Tax Law § 471(1). Federal law forbids the collection of these taxes on cigarettes sold on Native American reservations to enrolled tribal members for their personal consumption. See Moe v. Confederated Salish & Kootenai Tribes of Flathead Reservation, 425 U.S. 463 (1976). However, when cigarettes are sold on the

⁴ At the time of the acts alleged in the indictment, "contraband cigarettes" was defined to mean a quantity in excess of 60,000 cigarettes which bore no evidence of the payment of state cigarette taxes. The statute was amended in March 2006 and the number required to trigger the provisions of the CCTA was reduced to 10,000.

Parenthetically, there are 20 cigarettes in a pack and 10 packs in a carton; thus, 60,000 cigarettes equates to 300 cartons.

reservation to non-Native Americans, the taxes may be collected. See Washington v. Confederated Tribes of Colville Indian Reservation, 447 U.S. 134 (1980).

In sum, a sale of unstamped cigarettes (with the exception of on-reservation sales to a Native American for his or her own consumption⁵ and other exceptions not presently relevant), is violative of New York Tax Law § 471(1) and, to the extent such a sale exceeds 60,000 cigarettes, it violates § 2342(a). Conversely, a sale of unstamped cigarettes in a lesser amount is not a matter of federal concern in the sense it does not run afoul of federal law.

Positions of Parties

1. Government's Position

The government seeks "a money judgment from the Defendant for the gross proceeds of the RICO enterprise, or approximately \$172,000,000." (Gov't's Mar. 13, 2009 Letter Br. at 1; see also Gov't's June 8, 2009 Supplemental Mem. of Law Regarding Certain Forfeiture Issues ("Gov't's June 8, 2009 Suppl. Mem.") at 7 and Gov't's June 15, 2009 Reply Mem. of Law Regarding Certain Forfeiture Issues ("Gov't's June 15, 2009 Reply Mem.") at 9.) This sum represents the "total amount of the gross sales of

⁵ For a discussion of this exemption vis-a-vis the defendant's obligation at trial to come forward with evidence suggesting its applicability and the concomitant issue of the ultimate burden of proof, see this Court's February 26, 2009 Am. Memorandum and Order at 110-16.

the enterprise for [the period from January 1, 2000 through August 4, 2004]"⁶ as evidenced by government's exhibit 228. (Gov't's June 8, 2009 Suppl. Mem. at 3.)

While steadfastly adhering to the position that \$172,000,000 represents the appropriate number for forfeiture purposes, the government also presented information at the forfeiture hearing pertaining to an alternate theory of recovery. That alternate theory is based, not on the total cigarette sales for the relevant period, but on the CCTA sales which the government estimates to be \$33,503,139.86. (See Gov't's Ex. 231.)⁷ The 33 million plus figure is the result of the government reviewing the Peace Pipe sales records for 6 of the 40

⁶ Although the indictment charges that the Count Two racketeering conspiracy extended from "[i]n or about and between October 1996 and September 2004," the government's proof concerning the CCTA sales at trial and during the forfeiture hearing was limited essentially to the January 1, 2000 to August 4, 2004 period, i.e. from the first full year reflected in Peace Pipe's "software accounting program . . . record[ing] sales [and] purchases" installed in "late . . . 1999" (May 28, 2009 Tr. at 9-10), until the execution of the search warrant on August 4, 2004.

⁷ In its June 15, 2009 Reply Memorandum, the government states that the "approximate amount of CCTA sales is \$50,000,000," citing government's exhibit 272e. (June 15, 2009 Reply Mem. at 6.) However reference to government exhibit 272e, viewed in conjunction with government's exhibit 231, indicates the \$50,000,000 figure represents the total cigarette purchases by Peace Pipe's "Big Customers," i.e. those purchasing \$10,000 or more of product during the January 1, 2000 to August 4, 2004 period, rather than the amount of CCTA purchases included within that figure. Which is to say, the CCTA amount as per the government should read \$33,503,139.86, not \$50,000,000. (Gov't's Ex. 231.)

customers who purchased over \$100,000 of unstamped cigarettes from the Enterprise during the previously referenced period, and determining the percentage of their total purchases which constituted CCTA purchases, i.e. purchases in excess of 60,000 cigarettes at a time. That percentage is approximately 66.99%. (See May 28, 2009 Tr. at 49 and Gov't's Ex. 231.) The percentage was then applied by the government to the other 34 entities which spent in excess of \$100,000 as well as to other big customers which fell within the following categories: "\$10,000-\$25,000," "\$25,000-\$50,000," and "\$50,000-\$100,000." (Gov't's Ex. 231.) Based on that process, the government estimates the total CCTA sales to be \$33,503,139.86.

As explained infra, defendant maintains that after the gross amount subject to forfeiture is determined, the cost of goods sold must be deducted.⁸ In response, the government contends, in categorizing what it incorrectly perceives to be the defendant's argument, that "even if net profits were the appropriate measure,⁹ which it is not, the Defendant, not the Government, bears the burden of proving costs" which burden he

⁸ The cost of goods sold deduction sought by the defense from the gross proceeds generated by CCTA sales is limited to Peace Pipe's direct costs, viz. what it paid to its suppliers for the cigarettes involved.

⁹ Defendant argues that "gross profits," not net profits, are the appropriate measure. (Def.'s June 8, 2009 Letter Br. at 4.)

has not met. (Gov't's June 15, 2009 Reply Mem. at 8.)

2. Defendant's Position

Defendant maintains that any sum subject to forfeiture must be related to a CCTA violation and, therefore, the government's principal argument calling for the forfeiture of all of the sales proceeds arising from Peace Pipe's marketing of unstamped cigarettes, whether constituting CCTA violations or otherwise, necessarily suffers from overbreadth.

As to the government's fall-back position, defendant contends:

The government's estimate that CCTA sales totaled \$33,503,139.86 is grossly inaccurate, for two principal reasons. First, Agent Wanderer's^[10] average figure of 66.99% was calculated without regard to the 0% figure for Tin Tin – even though Agent Wanderer testified, inaccurately, that "by including him in there, he actually pulled the rest of the percentages down" (Tr. 53 ["Tr." references are to the May 28, 2009 transcript unless otherwise noted]). Had the government in fact included Tin Tin in the averaging process – and there was no reason to not do so – then Agent Wanderer's inaccurate 66.99% figure is reduced to 55.67%.

The government's percentage estimate is inaccurate for the additional reason that it assumes that the purchases of the smallest purchasers were as likely to be in CCTA quantities as purchases of the largest purchasers. Not only is this counter-intuitive, but also Agent Wanderer's own Exhibit 231 suggests otherwise. Taken from Exhibit 231, the six "large customers" analyzed by Agent Wanderer had the following Total Purchases, CCTA Purchases and resulting "CCTA

¹⁰ Robert Wanderer, a United States Internal Revenue Service Agent with "approximately 36½ years" experience was the sole witness at the May 28, 2009 forfeiture hearing. (May 28, 2009 Tr. at 7.)

purchases as a % to total purchases," in descending order of total purchases:

Customer	Total Purchases	CCTA Purchases	% CCTA
Rueben	\$857,659.30	\$674,763.50	78.68
Alz Alz	\$531,209.00	\$445,337.00	83.83
Ms Tiny	\$497,499.60	\$323,338.10	64.99
Chike Ramsay	\$368,530.90	\$196,821.45	53.41
Sand	\$228,581.35	\$121,425.25	53.12
Tin Tin	\$146,339.00	\$0.00	0
Totals	\$2,629,819.15	\$1,761,685.30	55.67

The numbers in the table reflect a clear downward trend in the ratio of CCTA purchases to total purchases as the total purchases by customer decreases, and logically this trend would continue, or even accelerate, as other customers, with even smaller total purchases, are considered; after all, the largest customers would likely make a larger percentage of large wholesale purchases (as in fact is reflected in the table). Yet rather than attempting to factor this trend into its calculations the government simply assumes the same (inaccurate) percentage of CCTA purchases was made by the smallest of the "big" customers (i.e. those 2,113 customers each spending a total of \$10,000-25,000 [see Exhibit 232]) as those 40 customers each spending in excess of \$100,000 (see Exhibit 232).

(Def.'s June 8, 2009 Letter Br. at 2-3 (footnote omitted).)

Defendant opines that the total amount of CCTA sales should be determined by focusing solely on purchases made by those big customers who spent \$100,000 or more. Purchases by that group totaled \$9,136,092.53. (Gov't's Ex. 232.) That sum multiplied by defendant's 55.67% produces a CCTA revenue figure of \$5,086,092. From that, the argument continues, the cost of goods sold – which defendant estimates to be approximately 85% –

should be deducted, producing a forfeitable amount of \$767,909.30 representing the gross profit realized by the Peace Pipe from its CCTA sales.

And finally, on the issue of burden of proof, the defendant insists that the cost of goods sold represents part of the government's burden of proof, particularly, in his view, given that both the government and the defense have access to the same information, i.e. the defendant's financial records seized during the execution of the search warrant on August 4, 2004.

Issues to be Resolved

1. Is the government entitled to a money judgment equal to the total gross receipts received by the Peace Pipe from all cigarette sales during the relevant time period, or only those receipts attributable to CCTA sales?

2. Once the nature of the proceeds subject to forfeiture is determined, should a deduction be made from the resulting gross figure for cost of goods sold?

3. If so, does the defendant have the burden of going forward on the issue, if not the burden of proof, or is it the government's burden to prove, not only the gross receipts, but also the amounts to be deducted therefrom as cost of goods sold?

DISCUSSION

1. Proceeds Subject to Forfeiture are Limited to Those Derived From CCTA Sales

As noted, the government maintains that it is entitled to a monetary judgment commensurate with the \$172,000,000 gross revenues generated by the Peace Pipe from the sale of cigarettes not bearing tax stamps as required by New York Tax Law § 471(1). The theory underlying that demand is that since Russello v. United States, 464 U.S. 16 (1983) instructs that "proceeds" are an "interest" for purposes of § 1963(a)(1), and given that a defendant's interest in an enterprise is forfeitable in toto, ergo so are the proceeds generated by the enterprise even if, as here, some portion of those proceeds were derived from activities which did not violate federal law per se nor constitute racketeering activity under § 1961(1).

While a defendant's "entire interest in [a] RICO enterprise [is forfeitable, independent] of the enterprise's [degree] of criminal taint," United States v. Walsh, 700 F.2d 846, 857 (2d Cir. 1983), it does not follow that Morrison may be legitimately saddled with a personal judgment based on sales not derived from racketeering activities. Which is to say, the "indivisib[ility]" rule applicable to a defendant's interest in a RICO enterprise, id., is not applicable for present purposes.

The government's request was initially identified as premised on "§§ 1963(a)(1) and (a)(3)." (Gov't's Mar. 6, 2009

Mem. at 1.) However, elsewhere in its submissions references to § 1963(a)(2) appear. (See Gov't's June 15, 2009 at 2.) Before discussing those three subdivisions of § 1963(a), it is important to focus on precisely what the government is seeking and not seeking by way of forfeiture.

While Morrison is not an owner of Peace Pipe, he, with his spouse, is a partner in its operation. (Gov't's Ex. 159a.) As such, he presumably has an "interest" in the Enterprise for purposes of § 1963(a). Yet, the prosecution has not asked for a money judgment matching the value of that interest (whatever it may be), as distinct from a money judgment based on the gross sales, i.e. "proceeds" generated by the Enterprise. With that recognition in mind, attention is now directed to subdivisions (a)(1), (a)(2), and (a)(3) insofar as each relates to the government's specific request.

18 U.S.C. § 1963(a) provides that a defendant who violates any provision of section 1962 shall forfeit:

- (1) any interest the person has acquired or maintained in violation of section 1962;
- (2) any-
 - (A) interest in;
 - (B) security of;
 - (C) claim against; or
 - (D) property or contractual right of any kind affording a source of influence over;

any enterprise which the person has established, operated, controlled, conducted,

or participated in the conduct of, in violation of section 1962; and

- (3) any property constituting, or derived from, any proceeds which the person obtained, directly or indirectly, from racketeering activity or unlawful debt collection in violation of section 1962. . . .

18 U.S.C. § 1963(a).

The pivotal distinction between the forfeiture of proceeds and the forfeiture of a defendant's interest in an enterprise vis-a-vis linkage to racketeering activity is found in the following excerpt from United States v. Anquilo:

The types of property interests subject to forfeiture under § 1963 can be divided into two broad categories: (1) interests in a RICO enterprise, and (2) interests outside the enterprise. Any interests in an enterprise, including the enterprise itself, are subject to forfeiture in their entirety, regardless of whether some portion of the enterprise is not tainted by the racketeering activity. As the Ninth Circuit stated in United States v. Busher, 817 F.2d 1409 (9th Cir. 1987): "[F]orfeiture is not limited to those assets of a RICO enterprise that are tainted by use in connection with racketeering activity, but rather extends to the convicted person's entire interest in the enterprise." Id. at 1413.

The forfeiture of interests outside the enterprise, however, is subject to limitations. It has been held that the forfeiture of outside interests is subject to a rule of proportionality. See United States v. Porcelli, 865 F.2d 1352, 1362-65 (2d Cir.), cert. denied, 493 U.S. 810, 110 S.Ct. 53, 107 L.Ed.2d 22 (1989); United States v. Horak, 833 F.2d 1235, 1242-43 (7th Cir. 1987). Such outside interests include proceeds or profits forfeitable under §

1963(a)(1), see, e.g., Horak, 833 F.2d at 1242-43. . . . This is in contrast to the treatment of interests in an enterprise, which are forfeitable regardless of percentage of taint.

897 F.2d 1169, 1211-12 (1st Cir. 1990). See also Porcelli, 865 F.2d at 1364-65 (distinguishing between RICO enterprise which is "indivisible and is forfeitable in its entirety" and interests outside the enterprise which are forfeitable under § 1963(a)(1) only to the extent they were derived from racketeering activity).

The distinction between subsections (a)(1) and (a)(2) was further explained in Horak:

Section (a)(1) focuses on the racketeering activity and divests the convicted defendant of all interests "acquired or maintained" by that activity. It is apparently irrelevant whether such interests are part of the charged enterprise. Section (a)(2), on the other hand, as discussed below, focuses on the enterprise, not the specific racketeering activity, and divests the convicted defendant of all interests in the enterprise. It would therefore seem irrelevant (at least in terms of the structure of the statute) whether (a)(2) interests were directly related to the racketeering activity of which the defendant was convicted.

833 F.2d at 1243 (emphasis in original).

As to subsection (a)(3), the statutory language, as well as the legislative history accompanying its enactment, compels the conclusion that a nexus must exist between the property sought to be forfeited and one or more racketeering

acts. Thus subsection (a)(3) provides in pertinent part that "any property constituting, or derived from, any proceeds which the person obtained, directly or indirectly, from racketeering activity or unlawful debt collection in violation of section 1962" is subject to forfeiture. 18 U.S.C. § 1963(a)(3) (emphasis added). And, as noted in subsection (a)(3)'s legislative history:

TO COME WITHIN THE SCOPE OF PARAGRAPH (3), PROPERTY MUST CONSTITUTE, OR BE DERIVED FROM, PROCEEDS THE DEFENDANT OBTAINED THROUGH THE RACKETEERING ACTIVITY INVOLVED IN THE RICO VIOLATION. THUS, PROCEEDS ACCRUING TO AN ENTERPRISE OR ASSOCIATION INVOLVED IN A RICO VIOLATION WILL BE FORFEITABLE ONLY TO THE EXTENT THAT THEY ARE DERIVED FROM RACKETEERING ACTIVITY OR UNLAWFUL DEBT COLLECTION. FOR EXAMPLE, IF ONLY PART OF A CORPORATION'S AFFAIRS WERE CONDUCTED THROUGH A PATTERN OF RACKETEERING ACTIVITY, THE GAIN PRODUCED THROUGH THIS ACTIVITY WOULD BE SUBJECT TO FORFEITURE BUT THE LEGITIMATELY PRODUCED PROFITS OF THE CORPORATION WOULD NOT.

S. Rep. 98-225, at 199 (1983), reprinted in 1984 U.S.C.C.A.N. 3182, 3382 (footnote omitted) (emphasis added).

Given that the prosecution is seeking a money judgment based on Peace Pipe's total cigarette sales, its application is governed by the rules relating to proceeds under subsections 1963(a)(1) and (a)(3). That does not mean that the government must establish a specific "nexus between the property and the offense" since it is not seeking forfeiture of "specific propert[ies]," Fed. R. Crim. P. 32.2(b)(1); it does mean,

however, the government must demonstrate that the amount of the requested money judgment is commensurate with the proceeds attributable to racketeering activity.¹¹ Indeed, the government acknowledges as much in one of its written submissions. (See Gov't's Mar. 6, 2009 Mem. at 4 ("The Government . . . is entitled to a judgment against the defendant for an amount of money equal to the value of the proceeds of the racketeering activity.")).¹²

Here the "racketeering activity" which is part and parcel of the RICO conspiracy conviction and the lone predicate for RICO forfeiture is found in "sections 2341-2346 (relating to trafficking in contraband cigarettes)." 18 U.S.C. § 1961(1). To argue, as the government does, that "the Defendant was not convicted of CCTA violations [but] of conducting the affairs of a criminal enterprise" and, thus, the proceeds from all cigarette

¹¹ To the extent the government argues that all of the proceeds of the Peace Pipe are forfeitable because "[a]ll of the Defendant's cigarette sales were unlawful [under N.Y. Tax Law § 471(1)]," (Gov't's June 15, 2009 Reply Mem. at 7), the government conflates illegal activity with racketeering activity which are not necessarily synonymous. As noted above, only proceeds that are derived from racketeering activity are forfeitable under subsections (a)(1) and (a)(3).

¹² Since RICO forfeiture is a sanction against the individual, in personam, and not against a particular asset, the Government is not obligated to trace the path of illegal proceeds. See United States v. Robilotto, 828 F.2d 940, 948-49 (2d Cir. 1987). In other words, it "does not matter whether the government recovers the identical dollars that the defendant received in violation of section 1962, as long as the amount that the defendant acquired in violation of the statute is known." United States v. Ginsburg, 773 F.2d 798, 801 (7th Cir. 1985) (en banc).

sales are subject to forfeiture (Gov't's Apr. 17, 2009 Reply Mem. of Law Regarding Certain Forfeiture Issues at 2), confuses the forfeitability of a defendant's interest in an enterprise with the forfeitability of the proceeds generated by that enterprise; as to the latter, the proceeds must, for the reasons indicated, be tethered to a § 1961(1) racketeering activity to be forfeitable under § 1963(a). Only a portion of the subject \$172,000,000 satisfies that condition.¹³

2. Peace Pipe's Sales of Contraband Cigarettes
During the January 1, 2000 - August 4, 2004
Time Period are Estimated to be \$6,120,268.39

Having determined that the Peace Pipe proceeds are divisible for purposes of forfeiture, the question becomes how much of Peace Pipe's total sales of unstamped cigarettes

¹³ To the extent the government cites United States v. Fruchter, 411 F.3d 377 (2d Cir. 2005) and United States v. Capoccia, 503 F.3d 103 (2d Cir. 2007) for the proposition that all proceeds generated by the enterprise are forfeitable - including those unrelated to racketeering activity - because defendant was convicted of a RICO conspiracy, the government is mistaken. Fruchter held that acquitted conduct could form the basis for a forfeiture of "'proceeds' derived from racketeering activity," 411 F.3d at 384 (quoting 18 U.S.C. § 1963(a)(3)), provided that the court finds by a preponderance of the evidence that such activity was reasonably foreseeable to the defendant. See also Capoccia, 503 F.3d at 117-18 ("[W]e have held that a defendant may be required to forfeit all proceeds of the racketeering enterprise forming the basis of his conviction, including proceeds of particular racketeering activities of which the defendant was not convicted.") (emphasis added). These cases do not hold that all proceeds are forfeitable. In fact, the quoted language supports the opposite conclusion, viz. only "proceeds derived from racketeering activity" are forfeitable. Fruchter, 411 F.3d at 384 (internal quotation marks and citation omitted).

represented CCTA sales. Primarily it should be noted that the type of analysis now being undertaken does not have to be resolved with certitude; rather a reasonable estimate is permissible. United States v. Lizza Indus., Inc., 775 F.2d 492, 498 (2d Cir. 1985).

The amount forfeitable per the RICO conspiracy conviction is not limited to the CCTA racketeering acts listed in the indictment. See United States v. Capoccia, 503 F.3d 103, 117-18 (2d Cir. 2007). Defendant does not contend otherwise. Instead, he recommends, to partially reiterate, a three step process for appropriately resolving the forfeiture issue. Step one calls for calculating Peace Pipe's total sales to its 40 big customers who purchased over \$100,000 of cigarettes during the subject period. That amount, \$9,136,092.53, should then be multiplied under step two by defendant's CCTA percentage of 55.67%,¹⁴ resulting in a gross CCTA sales figure for the 40 big customers of \$5,086,062. From that sum, the cost of goods sold should be deducted to reflect gross profits of \$767,909.30 which, in defendant's view, represents the maximum permissible

¹⁴ The government's 66.99% was derived by dividing the total CCTA purchases of the six big customers listed in government's exhibit 231, \$1,761,685.30, by the total cigarette purchases of the same six customers, \$2,629,819.15. That methodology more accurately portrays the pivotal relationship between the CCTA and non-CCTA cigarette sales at least as to these six customers than the defendant's method of simply averaging the averages independent of the various quantities purchased by the six big customers.

forfeiture award.

Initially, it warrants underscoring that Agent Wanderer ("Wanderer") testified that he could have "asked for [and received] detailed histories" for all of Peace Pipe's big customers providing their respective CCTA purchases, not just for the six listed in government's exhibit 231. (May 28, 2009 Tr. at 65-66; see also id. at 67 (indicating the absence of such information for "the three categories below a hundred thousand; namely categories 50 to 100, . . . 25 to 50, and . . . 10 to 25").)

The government's attempt to fill that void by seeking to apply its 66.99% figure to all of the 2,426 big customers, defined as those spending over \$10,000 or more (Gov't's Ex. 232), results in a gross overestimation of Peace Pipe's CCTA sales based on the evidence presented. For example, there is no reason to believe that that percentage pertains to customers who, rather than spending in excess of \$100,000, spent between \$10,000 and \$25,000 in purchases from Peace Pipe during the four year, seven month period given that the government's estimated minimum price for a CCTA purchase is \$6,200.¹⁵ For customers in that bottom

¹⁵ The \$6,200 CCTA purchase figure was based on the price charged to the largest of the big customers. (May 28, 2009 Tr. at 80.) However, the evidence demonstrates that the corresponding number for lesser customers was, at least in some instances, considerably higher than \$6,200. (Id. at 78-82.) Simply put, \$6,200 is the "smallest purchase that qualifies as a CCTA purchase." (Id. at 59.)

bracket of the big customer spectrum with average per customer purchases of "13,966.08" (Gov't's Ex. 232), one trip to the Peace Pipe per year, or roughly four trips, would result in average purchases well under the \$6,200 threshold. That circumstance, viz. average purchases beneath the CCTA sales threshold is not, of course, incompatible with CCTA sales having occurred but, all other things equal, does significantly lessen the likelihood that the 66.99% figure is applicable to customers within this bracket. Moreover, the above information viewed in conjunction with other evidence in the record, demonstrates that the government has also failed to establish that some lesser percentage is applicable to individuals who spent between \$10,000 and \$25,000 at the Peace Pipe. Reference to government's exhibit 272f, entitled "BIG CUSTOMERS," shows the "[t]otal [s]ales" for each customer in the \$10,000 to \$25,000 bracket, together with that customer's "[t]otal [v]isits" to the Peace Pipe. (Gov't's Ex. 272f at 6 to 17.) The lowest number of visits recorded for a customer is 8, with high double and triple digit visits per customer being commonplace. Simply opining, as Wanderer did, that it "is reasonable [to assume] that there could be CCTA [purchases]" in that bracket falls far short of proving, approximately or otherwise, the existence of CCTA sales particularly in view of the frequency with which the individual customers went to the Peace Pipe. (May 28, 2009 Tr. at 64 (emphasis added).)

The same infirmity is found in the \$25,000 to \$50,000 bracket with 206 customers and an average total expenditure for the period of \$33,318.79. (Gov't's Ex. 232.) Six visits during the time frame would bring the average expenditure per visit below the \$6,200 CCTA threshold, again lessening the likelihood that the customers involved in fact made CCTA purchases on one or more of their visits. Once again reference to government's exhibit 272f indicates that the vast majority of the number of visits per customer were in double or triple digits with the lowest being "5" with the corresponding total sales figure being "25,702.00," for an average expenditure of \$5,140.40. (Gov't's Ex. 272f at 6.) None of the average purchases per visit in this bracket reaches \$6,200. Thus, although there may have been some CCTA sales to members in this bracket, the proof fails to demonstrate that to be the fact.

The government's proof as to CCTA sales in the \$50,000 to \$100,000 bracket is similarly unpersuasive. Again, there is a failure to satisfactorily explain why the 66.99% figure, or any other percentage, is germane to this bracket. While the average purchase per customer during the period is \$67,194.89 for the 67 customers involved (Gov't's Ex. 232), the number of visits for each of those customers spans from 3 (Gov't's Ex. 272f at 2) to 1,560 (id. at 1), with most entries being in the mid to high double or triple digit range. With the exception of the average

purchase per visit for the one customer whose visits to the Peace Pipe were limited to 3, none of the other customers in this bracket had an average approaching \$6,200.

In sum, the proof fails to substantiate the government's claim that 66.99% of the customers in the \$50,000 to \$100,000 bracket, or some meaningful lesser percentage purchased CCTA amounts – i.e. over 60,000 unstamped cigarettes at a time – from the Peace Pipe during the relevant time period. The same, as explained supra, may be said of the other categories below that range, viz. the \$10,000 to \$25,000 and \$25,000 to \$50,000.¹⁶

The deficiencies in proof plaguing the above three categories are not found in the \$100,000 plus bracket. As to that bracket, the government counted the actual number of CCTA sales during the relevant time frame for six of the biggest customers, and then extrapolated the resulting percentage of CCTA to total cigarette sales to that bracket's other 34 big customers. I accept that process as providing a reasonable estimate of gross proceeds realized by the Peace Pipe from its CCTA sales to customers in the \$100,000 plus category. In that

¹⁶ This conclusion is further bolstered by the fact that, as defendant points out, "[t]he numbers in [government's exhibit 231 regarding the percentage of CCTA purchases of six big customers] reflect a clear downward trend in the ratio of CCTA purchases to total purchases as the total purchases by customer decreases, and logically this trend would continue, or even accelerate, as other customers, with even smaller total purchases, are considered" (Def.'s June 8, 2009 Letter Br. at 3.)

regard, it warrants mention that the government's total amount of cigarette sales to the forty customers in that bracket, together with the non-CCTA and CCTA cigarette sales made to each of the aforementioned six customers and concomitant individual percentages between the two types of sales, are all incorporated into the first step of the defendant's forfeiture argument; his objections are confined to the prosecution's combined 66.99% figure, and the application of that, or any other percentage to the other three, lesser categories. The Court has rejected the first of these arguments, and accepted the second. In any event, for the reasons indicated, I find that the total CCTA sales of the Peace Pipe were approximately \$6,120,268.39 ($\$9,136,092.53 \times 66.99\%$).

Attention will next be directed to defendant's position that the cost of the CCTA cigarettes to the Peace Pipe should be deducted from the gross receipts realized from their sale to obtain the amount subject to forfeiture.

3. ALTHOUGH IT APPEARS THAT IT WOULD BE APPROPRIATE TO DEDUCT WHAT PEACE PIPE PAID FOR THE CCTA CIGARETTES FROM THE CORRESPONDING GROSS SALES IN DETERMINING THE AMOUNT SUBJECT TO FORFEITURE, THE DEFENDANT HAS NOT MET HIS BURDEN OF COMING FORWARD WITH SUFFICIENT INFORMATION TO PERMIT THE COURT TO MAKE THE REQUESTED DEDUCTION

Should the sums paid by the Peace Pipe to its suppliers for the product sold to the CCTA purchasers be deducted from the gross proceeds generated by CCTA sales? While the answer to that

question is not free from doubt, such Second Circuit authority as there is suggests that such a deduction would be appropriate.

See Lizza, 775 F.2d at 497-99. Here, I would be prepared to make the deduction if there was adequate evidence before me to do so. However, that is not the case.¹⁷ That brings us to the question of which party suffers the consequences of the subject deficiency.

The government opines that the cost of goods sold is an affirmative defense to be established by defendant. Defendant counters that the burden of proof rests with the government not only as to the gross CCTA sales but also as to the cost of goods sold since, in defendant's view, only gross profits are subject to forfeiture. And, even if, arguendo, the burden of proof rests with the defendant, defendant maintains he met that burden in

¹⁷ My initial impression that the amount Peace Pipe paid to its cigarette suppliers should be readily determinable from its financial records was quickly dispelled upon discovering the creative accounting techniques utilized in the business to determine profitability. For example, reference to government's exhibit 224, entitled "Profit and Loss [for the period] January through December 2000" shows sales of \$27,730,788.34 but a minus "Net Income" figure of "\$1,302,858.75." Among the major unfathomable charges against total sales are such otherwise unexplained items as \$3,921,084.90 for "RAM, Sr. Personal," \$133,178.07 for "Charolette Morrison Personal," \$2,685,105.85 for "Investment," and even "Victoria's Secret \$316.50." (Gov't's Ex. 224.) The use of such bizarre deductions in calculating what is identified in the Profit and Loss statement as the business' "Net Income" necessarily undermines the confidence the reader might otherwise be prone to place in such entries on Peace Pipe's financial records as "cost" and "cost of goods sold."

that a number of the schedules received in evidence delineate the cost of the CCTA cigarettes sold by the Peace Pipe.

The government cites United States v. Schlesinger, 396 F. Supp. 2d 267, 278 (E.D.N.Y. 2005), aff'd 514 F.3d 277 (2d Cir. 2008), in support of its position. In Schlesinger, Judge Spatt of this Court held that "[w]hile the government bears the initial burden of proving, by a preponderance of the evidence, the amount forfeited, pursuant to § 981(a)(2)(B) the defendant has 'the burden of proof with respect to the issue of direct costs'" Id. at 278 (quoting 18 U.S.C. § 981(a)(2)(B)). As noted in the above excerpt from Schlesinger, the operative statute expressly places the burden upon the defendant unlike § 1963 which is silent on the subject. Thus, while Schlesinger may provide some support for the government's position, that support is meager. The following excerpt from the Third Circuit's RICO forfeiture decision in United States v. Ofchinick, however, is instructive:

If direct costs need to be taken into account, it is the defendant who has the burden of going forward on this issue (if not the burden of proof, an issue we do not reach). The government should not have to prove the absence of direct costs in a case in which the defendant has not pointed to costs that might be deductible.

883 F.2d 1172, 1182 (3d Cir. 1989).

Morrison, unlike Ofchinick, did point out proffered direct cost deductions in various exhibits introduced by the

government during the May 28, 2009 forfeiture hearing, although the arguments advanced by defendant as to those exhibits lack merit. By way of example, defense counsel, referencing government's exhibit 228, a Peace Pipe "Profit and Loss" statement for the period from January 1, 2000 through August 4, 2004, argues "that to the extent that [the government relied upon Peace Pipe's] gross receipts figure [of] 170 – something million, . . . I don't think it is appropriate for the government to argue that . . . the court shouldn't rely upon other numbers within the very same document to show what the cost of the goods was." (May 29, 2009 Tr. at 29-30.) The total sales proceeds listed in government's exhibit 228 are \$172,202,235.63 with the corresponding "Cost of Goods Sold" being \$135,897,186.12, resulting in "Gross Profit" of \$36,200,875.03. While defendant's argument might have merit in a different factual context, it doesn't here for the reason mentioned in footnote 17 relating to the atypicality of the business' records. Under the present circumstances, the government is entitled to rely on Peace Pipe's reported total CCTA sales figure in government's exhibit 228 as an admission, while calling into question the legitimacy of the deductions defendant seeks to have made from that sum.

Defense counsel also points to government's exhibit 264 for the proposition that the record supports "an approximate calculation for cost of goods sold." (Def.'s June 8, 2009 Letter

Br. at 4.) That Exhibit provides a detailed purchase history for one of the six big customers, to wit Alz Alz, including Peace Pipe's corresponding "Sold Price" and "Cost" per transaction. While acknowledging that Agent Wanderer testified that he didn't know what items were included in such terms as "Cost" and "Costs of Goods Sold," i.e. whether those terms included more than what Peace Pipe paid for the subject cigarettes (see May 28, 2009 Tr. at 42, 46, 48), defendant maintains that "[n]othing suggests [that 'Cost'] means anything other than 'costs of goods sold'" consistent with defendant's requested deduction. (Def.'s June 8, 2009 Letter Br. at 5 n.4.) In support of this argument, defendant contends that there are "numerous instances" within Exhibit 264 "where the 'cost' remains at \$20.87 even though the 'sold price' increases from \$23.00 and \$23.50." (Id.) Defendant adds "[o]ne would think that if a percentage of other overhead were included in 'cost' then the cost would increase as the 'sold price' increases to include an additional portion of overhead." (Id.)

The flaw in defendant's argument is that he has selectively culled cost and sales figures which support his argument to the exclusion of the remainder of the record. Although there are examples in Exhibit 264 where "Cost" remains constant as the "Sold Price" increases (see, e.g., Gov't's Ex. 264 at 4), there are numerous others where "Cost" increases as

the "Sold Price" increases (see, e.g., id. at 8, 12), and even instances in which the "Cost" increases as "Sold Price" decreases. (See, e.g., id. at 14.) (Similar anomalies, out of sync with defendant's hypothesis, are found in government exhibits 265 through 269 which represent detailed purchase histories for the other five big customers.)

The defendant argues that to the extent the record is muddled as to the meaning of such pivotal terms in Peace Pipe's records as "cost" and "cost of goods sold" that is the government's problem, not his. While it is true that the government has access to the same raw information as the defense, that does not mean that the government has the same ability to decipher that information. Wanderer could not determine what some of the key terms meant, nor can this Court on the information provided. That I find the evidence concerning the requested deduction for direct costs nondecipherable should come as no surprise to the parties given the questions I asked of the witness and of counsel during the forfeiture hearing. Defendant, as the person who virtually micromanaged every significant aspect of the Peace Pipe's operations, surely could have called the business's accountant, bookkeeper, software programmer or other witness that he knew could provide the necessary clarification concerning the deduction he seeks. That observation takes us back to who has the burden of proof. In my judgment, the burden

of coming forward at the very least, if not the burden of proof rested with Morrison. Ofchinick, 883 F.2d at 1182; see generally 2 McCormick on Evidence § 336 (Kenneth S. Broun ed., 6th ed. 2006) (distinguishing burden of coming forward with burden of proof: former is burden "of producing evidence, satisfactory to the judge, of a particular fact in issue"; the latter is "the burden of persuading the trier of fact that the alleged fact is true"). Having failed to discharge the burden of coming forward, Morrison's requested deduction against gross CCTA sales is denied as essentially unknowable based on Peace Pipe's flawed financial records.

CONCLUSION

For the reasons indicated:

(1) the proceeds subject to forfeiture are limited to those derived from Peace Pipe's CCTA sales;

(2) such sales are estimated to be \$6,120,268.39; and

(3) no deduction will be made from the \$6,120,268.39 figure as requested by the defense given that defendant failed to met his burden of coming forward with sufficient information to permit me to estimate the appropriate amount to be deducted.

Therefore, on the date of, and as part of the defendant's sentence, the government shall be awarded a money

judgment against defendant in the amount of \$6,120,268.39 by way of forfeiture pursuant to 18 U.S.C. § 1963(a).

SO ORDERED.

Dated: September 10, 2009
Central Islip, New York

DENIS R. HURLEY, U.S.D.J.